HOW TO CALCULATE YOUR TAXABLE PROFITS

This Help Sheet gives you information to help you fill in boxes in:

- **the Self-employment Pages of your personal Tax Return, or**
- **the Trading Pages of the Partnership Tax Return and the Partnership Pages of your personal Tax Return.**

Except where specifically noted in this Help Sheet the box numbers on the Trading Pages of the Partnership Tax Return follow those on the Self-employment Pages of the personal Tax Return.

This Help Sheet explains about:

- accounting periods
- how business profits are taxed
- cost of sales
- allowable business expenses
- basis periods
- overlap profits and relief
- capital allowances and balancing charges
- commencements and cessations
- terminal loss relief
- partners' trading or professional profits.

More detailed information is available if you need it. The Help Sheet refers you to other sources.

You will come across the terms 'accounting period' and 'accounting date' in both the notes to the Tax Return and the Help Sheets. If you do not have accounts prepared for your business, you should read:

- 'accounting period' to mean the period for which you provide details of your business income and expenditure, and
- 'accounting date' to mean the date on which that period ends.

ACCOUNTING PERIODS

boxes 3.4 to 3.5 You will need to decide upon your accounting date - that is, the date to which your accounts are drawn up. Enter the first day covered by the accounts in box 3.4 and your accounting date in box 3.5. You can choose any convenient date: for example, the anniversary of the date you began your business or, in a seasonal business, a date when trade is slack and stocks are low. You are entitled to change to a different date if you want to. However, whatever date you choose, you will find your tax is easier to work out if you keep to it each year. And if you have just started in business, you may find 5 April is the best date to choose as it keeps your tax calculation simple.

Even if you do not have accounts prepared for your business every year, your taxable profit should still be worked out using generally accepted accountancy principles. The Notes for the Self-employment Pages and the following notes provide some practical advice on how to complete your Tax Return if you do not have accounts.

HOW BUSINESS PROFITS ARE TAXED

Profits which arise from carrying on trades, professions and vocations cannot usually be worked out by simply adding together the cash receipts of the business and deducting expenses paid out. This would show the business's cash flow, but it would not normally be a proper measure of its profits. To arrive at the profits it is necessary to draw up accounts using the methods which accountants have developed for dealing with income which has been earned but not received, expenses which have been incurred but not paid or paid but not fully used, and so on. And the profits arrived at using these methods - the commercial profits - have to be adjusted for tax purposes. This is because in arriving at the commercial profits some items of income or expenditure may be recognised which are not taxable, or tax deductible, and other special allowances may reduce the amount of profits which are taxable.

These guidance notes explain these principles as fully as possible, but they are not a comprehensive guide in all circumstances. If you are in doubt about the correct treatment of a particular item you should consult your Inland Revenue office or tax adviser.

COST OF SALES

box 3.33 Show as cost of sales the cost of raw materials and goods bought for resale which you used during this accounting period. Make sure you count creditors, that is items delivered to you but which you had not paid for at the end of the period. Do not count items you paid for in this period if they were included as creditors in your last accounts.

You should include the value of stock you had on hand and uncompleted work in progress at the start of the period (this must be the closing figure which you used in your last accounts), but exclude the value of stock and work in progress at the end. Value your stocks for resale and your work in progress at their cost to you or, if this happens to be lower, at the net price they will fetch when sold in the normal course of your business. Value consumable stores at their cost to you, or if they have deteriorated or become obsolescent at their net realisable value where this is lower. The Working Sheet on page 2 will help you decide how much you can claim.

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Goods and raw materials you bought this period	A	£
Plus stock and work in progress on hand at the start of this period	B	£
	box A *plus* box B C	£
Minus stock and work in progress on hand at the end of this period	D	£
Figure to enter in box 3.33	box C *minus* box D E	£

ALLOWABLE BUSINESS EXPENSES

Broadly speaking, you can deduct from your turnover all the costs you incur for the sole purpose of earning business profits. But you cannot deduct costs which you incur for a non-business purpose, such as your own personal expenses or drawings. And you cannot deduct capital costs, that is, the cost of buying fixed assets or intangibles, such as goodwill, which last for several years (or losses you suffer when you sell them). But you may be able to claim capital allowances on these capital costs. Additionally you cannot deduct costs which are recoverable under an insurance.

Business expenditure is allowed in your accounts for a period if it was incurred in earning turnover in that period even if you are not due to pay the money until later.

The amount to deduct is the amount of the expense which was used up during this period. This may not be the amount actually paid. For example, if you owe money at the end of the account - your trade creditors - it may be that this should be included in this account rather than later when it is paid. (Make sure you do not deduct any payments made in this account which you included as trade creditors in your last accounts.) But if you make a payment which is used up over two periods or more you should spread it in your accounts. For example, if halfway through the year you pay 12 months rent in advance for your business premises, only one half of the payment should be deducted this year, and the other half next year.

The Notes for the Self-employment Pages tell you where to include your expenses. There is a Table on page SEN5 to help you decide which expenses can or cannot be claimed in working out business profits for tax purposes.

Use of mileage rates to calculate car expenses

You may calculate your car expenses using a fixed rate per business mile provided that:

- the rate used does not exceed the appropriate Fixed Profit Car Scheme (FPCS) mileage rate for the car at the time it is used. These rates are published annually by the Inland Revenue. (The rates for 2000-2001 were announced in a press release dated 14 December 1999 and remain at their present level. The press release is available from the Orderline), **and**
- the annual turnover of the business at the time the car is acquired does not exceed the VAT registration threshold (currently £48,000), **and**
- no other motoring expenses (other than interest on a loan used to purchase the car) are claimed and no capital allowances are claimed on the car (since the FPCS rates already contain an element to allow for depreciation), **and**
- such a basis is applied consistently from year to year so that any change to or from an 'actual' basis (including one required by a change in turnover relative to the VAT registration threshold) takes place only when one car is replaced by another.

The VAT registration threshold is used here purely as a convenient limit whose real value is regularly reviewed; this practice has no application to VAT accounting and does not affect existing VAT rules and practices.

This practice does not apply to taxis and other cars used for hire, nor to vehicles other than cars.

If you have existing arrangements for the use of mileage rates other than those set out in this Help Sheet, your Inland Revenue office will expect that on the next change of vehicle, these arrangements are replaced either by claims to actual expenses or (where the conditions in this Help Sheet are satisfied) by claims in accordance with the practice set out in this Help Sheet.

Whatever your business and however you work out your motoring expenses, you must keep adequate records to back up your Tax Return. For more information ask the Orderline for booklet *SA Book 3: Self Assessment: A guide to keeping records for the self-employed*.

YOUR BASIS PERIOD FOR 2000-2001

You pay tax for 2000-2001 according to the profits, or losses, for your basis period. After the first year or two in business, your basis period will be the 12 month period you use for your accounts, except if you change your accounting date. However, you should check the following rules which enable you to work out your basis period. (Partnerships do not have basis periods. But the rules for changes of accounting dates apply. For information about partner's own basis periods, see pages 9 and 10.)

Your accounting period is the period your accounts cover; your accounting date is the last day of your accounts. For example, if you draw up accounts each year to 31 December, your accounting period for the 2000-2001 tax year is the 12 month period 1 January 2000 to 31 December 2000 and your accounting date is 31 December 2000.

GENERAL RULES FOR BUSINESSES STARTED IN 1997-98 OR EARLIER

If you started business before 6 April 1998 and you were still in business at 5 April 2001, your basis period is the 12 months to your accounting date in 2000-2001 unless you have changed accounting date during 2000-2001 - see 'Changes of basis period' in the next column.

Example 1
You started your business on 1 January 1997 and have drawn up accounts to 31 December 1997, 31 December 1998 , 31 December 1999 and 31December 2000. Your basis period for 2000-2001 is the 12 months 1 January 2000 to 31 December 2000.

COMMENCEMENT

Business started in 1998-99

If you started business during the period 6 April 1998 to 5 April 1999, your basis period is one of the following *unless you have changed accounting date during 2000-2001 - see 'Changes of basis period' in the next column.*

If your accounting date in 2000-2001 is 12 months or more after the date on which you started in business, your basis period is the **12 months to your accounting date.**

If your accounting date in 2000-2001 is less than 12 months after the date on which you started in business, your basis period is the **12 months beginning on the date you started.**

If you do not have an accounting date in 2000-2001, your basis period is the 12 month period **6 April 2000 to 5 April 2001.**

Example 2
You started in business on 1.1.99.

- If your accounting date is 31.3.2000, your basis period is 1.4.99 to 31.3.2000.
- If your accounting date is 31.10.99, your basis period is 1.1.99 to 31.12.99.
- If your first accounting date is not until 30.4.2000, your basis period is 6.4.99 to 5.4.2000.
- If you drew up an account to 31.3.99 but did not draw up an account to 31.3.2000, *see 'Changes of basis period' section in the next column.*

Business started in 1999-2000

If you started business during the period 6 April 1999 to 5 April 2000, your basis period is the period from the date you started to 5 April 2000.

Example 3
You started in business on 1.7.99. Your basis period is 1.7.99 to 5.4.2000.

CESSATIONS

If you ceased business during the period 6 April 2000 to 5 April 2001, your basis period is the period between the end of the basis period for 1999-2000 and the date on which your business ceased.

Example 4
Your business ceased to trade on 31 December 2000. Your 1999-2000 basis period ended on 30 April 1999. Your basis period is the 20 month period 1 May 1999 to 31 December 2000.

CHANGES OF ACCOUNTING DATE

There is a change of accounting date if:

- you have drawn up your accounts to a date which is not the same as the date used for tax purposes last year, **or**
- you intend to draw up accounts for more than 12 months and no accounting date falls in the 2000-2001 tax year, **or**
- you changed your accounting date last year, this was not accepted by the Inland Revenue office, and you have drawn up your accounts to the same date this year. (But if you have changed back to your old date this is not treated as a change of accounting date.)

You will normally want your new accounting date to count for tax - otherwise your basis period will not end on the same date as your accounts. However, if you intend this to be only a temporary change, you may wish to ignore it for tax purposes. You can then work out your tax using the same basis period as last year.

Changes of basis period: special rules which apply if you change your accounting date

The notes above explain when a change of accounting date takes place for tax purposes. If you are in any doubt whether your accounting date has changed according to these rules, you should contact your Inland Revenue office or tax adviser for help.

When you change accounting date, and you want it to count for tax purposes, then your basis period will be given by one of two rules:

- if your accounting date in 2000-2001 is more than 12 months after the end of the basis period for 1999-2000, your basis period is the period between the end of the basis period for 1999-2000 and the new accounting date.

Example 5
If the basis period for 1999-2000 ended on 31 May 1999, and the new accounting date is 31 August 2000, your basis period is the 15 month period 1 June 1999 to 31 August 2000.

- if your accounting date in 2000-2001 is less than 12 months after the end of the basis period for 1999-2000, your basis period is the 12 months ending on the new accounting date.

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Example 6
If the basis period for 1999-2000 ended on 31 December 1999, and the new accounting date is 31 July 2000, your basis period is the 12 month period 1 August 1999 to 31 July 2000. (See also the section on overlap profit.)

Time limit for notifying the change of accounting date

If you wish a change of accounting date to count for tax purposes, you are required to let your Tax Inspector know in your Return, and give the reasons why the change has been made (box 3.8A is provided for you to notify the change).

One of the conditions for changing your basis period is that your Tax Return is sent back by the relevant filing date. If you fail to do this, the change of accounting date will not count for tax purposes.

WHAT TO DO IF YOUR BASIS PERIOD IS NOT THE SAME AS YOUR PERIOD OF ACCOUNT

Your basis period for 2000-2001 may be different from the period (or periods) for which your accounts are made up. If so, you must calculate the profit of the basis period by adding together and/or dividing the periods for which you have accounts. But see the note below if your accounting date falls between 31 March and 4 April.

Example 7
You commenced on 6 April 2000 and your basis period is the 12 months to 5 April 2001. But your accounts are made up for the three months to 30 June 2000 (profit £4,500) and the 12 months to 30 June 2001 (profit £24,000). So your basis period covers three months of your 2000 accounts and nine months of your 2001 accounts.

The profit of the basis period will be:
£4,500 + (279/365 x £24,000) = £22,500.

These calculations should strictly be made in days but weeks, months or fractions of years may be used instead.

ACCOUNTING DATES BETWEEN 31 MARCH AND 4 APRIL

The basis of assessment for the tax year in which a business commences (Year 1) is the profits arising in that tax year. So where a new business adopts an accounting date of 31 March and prepares its first trading accounts for a period of 12 months or less, it should in strictness:

- **if the business began on 6 April or later,** add on five days' worth of the profits of the following account in order to make up the full period to 5 April. There will therefore be an overlap of five days between the basis periods for Years 1 and 2, for which the 'overlap profit' should be calculated
- **if the business began on 1 to 5 April,** be taxed on one to five days' worth of the profits in Year 1. The basis period for Year 2 will be the first 12 months from commencement so that (except for businesses which began on 1 April) up to four days' worth of profits from the following account should be added on. There will again be overlaps between the basis periods for Years 1 and 2, and sometimes those for Years 2 and 3, for which the 'overlap profit' should be calculated.

However in either case, you can if you want, treat any apportionment of profit for a period of five days or less as zero (that is, all the profit will be treated as falling within the other part of the account). This will have the effect that:

- the profits of the account to 31 March each year will be taxed as though they were for the year to the following 5 April. Over the lifetime of the business, the full profits must, of course, be taxed
- for businesses which commence in the period 1 to 5 April, the taxable profits for Year 1 will be zero
- there will be no 'overlap profits', and hence no overlap relief in any later year.

This practice will not affect any other matters which depend upon the date on, or tax year in, which the business commences.

You may also treat a change of accounting date where the new date is 31 March as though it was a change to 5 April. All previous overlap profits will accordingly be deductible in the year the change takes effect for tax purposes. If you are in any doubt, ask your Inland Revenue office or tax adviser for help.

OVERLAP PROFITS

It may be that your basis period for 2000-2001 overlaps with the basis period for 1999-2000. Such overlaps can occur in the first three years after a business starts up, or in a year in which there is a change of basis period (because your accounting date has changed).

Example 8
Your business started on 1 January 2000, and your first account is for the 12 months to 31 December 2000. Your basis periods are:

1999-2000: 1 January 2000 to 5 April 2000
2000-2001: 1 January 2000 to 31 December 2000

The period of overlap is 1 January 2000 to 5 April 2000. So if the profit of the 12 months to 31 December 2000 is £12,000, the overlap profit is (95/365 x £12,000) = £3,123 (over 95 days). This is the same as the amount which was assessable for 1999-2000.

If your basis periods for 1999-2000 and 2000-2001 overlap, you should keep a record of both the overlap profit and the overlap period. Any overlap profit you have is carried forward until such a time as you can claim overlap relief. The amount of your overlap profit to be carried forward should be entered in box 3.77 (or box 4.11 of the Partnership Pages).

OVERLAP RELIEF

box 3.76* Include in the adjustments you make in box 3.76 any overlap relief you are allowed to deduct for 2000-2001. The notes below will help you work out how much overlap relief to deduct.

Overlap profits which arose in 1999-2000 or earlier years can be deducted as overlap relief in working out your taxable business profits for 2000-2001 if:

- you sold or closed down your business in 2000-2001. All the overlap profits brought forward should be entered at box 3.75 (or box 4.9 of the Partnership Pages), **or**
- your basis period for 2000-2001 is more than 12 months long because you have changed your accounting date since last year. (This can only happen if you changed your basis period.) The amount of overlap profits allowed as overlap relief is in proportion to the length of your basis period in excess of 12 months and the length of your overlap period from earlier years. Example 9 below shows how this works.

* or box 4.10 of the Partnership Pages.

Example 9

You have overlap profit of £5,000 (over five months) from an earlier year. You change basis period. Your basis period is 14 months and you are therefore entitled to overlap relief. There are five months of overlap profit available. The relief is in proportion to the number of months by which the basis period exceeds 12 months (that is, two months) and the length of the basis period (that is, five months).

So the relief is:

2/5 x £5,000 = £2,000.

The balance of overlap profit £3,000 (over three months) is carried forward. You will claim this as overlap relief in a later year.

CAPITAL ALLOWANCES AND BALANCING CHARGES

In working out your business profits you must **not** deduct:

- the cost of buying, altering or improving fixed assets, **or**
- depreciation or any losses which arise when you sell them.

Instead, you can claim tax allowances called capital allowances. These are deducted to arrive at your taxable profits. An adjustment, known as a balancing charge, may arise when you sell an item, give it away or stop using it in your business.

Balancing charges must be added back to arrive at your taxable profits. These notes explain how you can work out these capital allowances and balancing charges.

— Partnership Tax Return

The partnership can claim capital allowances on assets owned by the partnership. It can also claim capital allowances on plant and machinery owned by one of the partners but which is used in the partnership's business.

What can you claim capital allowances on?

You can claim capital allowances for the cost of:

- plant and machinery such as vehicles, tools, ladders, computers and business furniture which belongs to you (see 'Plant and Machinery' on page 6)
- agricultural buildings, industrial buildings and certain other buildings
- patents, certain specialist types of 'know-how', scientific research, mineral extraction and dredging. Your tax adviser will claim these for you, if they apply.

If you buy on hire purchase, you can claim capital allowances on the original cost of the item; the interest or other charges count as business expenses and should be deducted at box 3.48.

You cannot claim for anything you have bought solely for private use, or the cost of land even if it is used for your business.

Value Added Tax

The purchase price of an asset on which capital allowances can be claimed sometimes includes VAT. If you are registered for VAT and can offset that VAT against your output tax when you make your returns for VAT purposes, you should only claim capital allowances on the net cost of the asset. In all other cases, and particularly if you are not registered for VAT, the VAT paid should be included in the capital expenditure on which you claim capital allowances.

How you make your claim

Enter in boxes 3.61 to 3.70 the amount you wish to claim. This should be the amount worked out from the rules set out in these notes. The examples show you what to do. If you need more help ask your Inland Revenue office or tax adviser. You will also need to consult them if:

- you do **not** want to claim the full amount of allowances, **or**
- someone else pays part of the cost (for example, by giving you a grant), **or**
- you had purchases from or sales to members of your family or other connected persons.

Periods of account

You should make a separate capital allowance computation for each period of account. If the period of account is longer than 18 months it should be split into shorter periods and separate capital allowance computations made for each of them. The first 12 months will form a period and each subsequent 12 month period, or period of less than 12 months, will form further periods.

For example, if the period of accounts is the 20 months to 31 August 2001 you should split it into 12 months to 31 December 2000 and 8 months to 31 August 2001.

If there is a gap between two periods of account you should add it to the first period of account. For example, if accounts are drawn up for the year to 31 December 2000 and the period 12 April 2001 to 31 December 2001 you should add the period 1 January 2001 to 31 March 2001 to the year ended 31 December 2000.

If there is an overlap between two periods of account the overlap period should be treated as part of the first period of account only. For example, if accounts are drawn up for the 15 months to 31 March 2001 and the year ended 31 December 2001 you should treat the period 1 January 2001 to 31 March 2001 as being part of the 15 months to 31 March 2001 only.

The annual rate of writing down allowance for plant and machinery is 25%. This is increased or reduced if the period of account is more or less than 12 months. For example, if the period of account is 6 months long the rate of writing down allowance is $^{6}/_{12}$ x 25% = 12½%.

Plant and Machinery

You can claim first year and writing down allowances for the cost of vans, cars, machines, scaffolding, ladders, tools, equipment, furniture, computers and similar items which you use in your business. Do not claim for the things it is your trade to buy and sell - these should be claimed as business expenses.

First year allowances are available for most expenditure on plant and machinery apart from expenditure on motor cars and on assets which you lease out.

The percentage to be used depends on when the item was bought, and where it is to be used, as follows:

	Rate of first year allowance
Most items acquired by small and medium sized businesses for use primarily in Northern Ireland (see Note 1)	100%
Information and communications technology expenditure	100%
Items acquired for use elsewhere	40%

If the asset is used only partly for business the first year allowance is reduced accordingly.

Note 1: the 100% first year allowance is not available for goods vehicles used in a haulage business and unauthorised expenditure on items for use primarily in agriculture and fishing businesses.

Most expenditure on plant and machinery incurred is lumped together in a single 'pool' of expenditure. There is a single capital allowance calculation for the pool no matter how many items are included. Where a first year allowance is claimed the balance of the expenditure after deducting the first year allowance is added to the pool for the following year. The types of plant and machinery which cannot be pooled are explained later in these notes.

Writing down allowances are worked out on an annual rate of 25% of the cost of the item or 'pool' of items for each year. Example 10 shows how this works.

Example 10

Your accounts are drawn up to 5 April each year. You spend £800 on a new machine in the year ended 5 April 2000. You do not buy anything in the year ended 5 April 2001.

The writing down allowance you can claim for 2000-2001 is:

Cost of machine	£800
Writing down allowance @ 25%	£200
Value of pool to carry forward	£600

The writing down allowance you can claim for 1999-2000 is:

Value of pool brought forward	£600
Writing down allowance @ 25%	£150
Value of pool to carry forward	£450

If you buy something in the period covered by your accounts and you do not claim first year allowance, the cost is added to the pool. If you claim first year allowance you cannot add anything to the pool until the following year when you can add the cost after deducting the first year allowance claimed. You can also bring into the pool the value of any items which you used privately before using them in your business. If you sell something, the sale proceeds (or the value if you gave it away or started to use it for non-business purposes) are deducted from the pool. If the sale proceeds etc. are more than the original cost of the asset you should deduct the original cost unless you acquired the asset from a connected person. If you did, you should deduct the greater of the cost to them and your cost if both of them are less than the sale proceeds. Once these adjustments have been made, your writing down allowance for those accounts is calculated.

If the sale price is more than the value of the pool, the difference is a balancing charge.

Example 11
Suppose that the value of the pool brought forward at the beginning of 2000-2001 was £450, that in your accounting period for 2000-2001 you bought a new machine for £500 in April 2000 and a new machine for £2,000 in August 2000, and you sold a machine on which you are claiming capital allowances for £150. Your capital allowance computation for 2000-2001 looks like this:

Cost of machine April 2000	£500
Cost of machine August 2000	£2,000
	£2,500
First year allowance @ 40%	£1,000
Value carried forward	£1,500
Pool brought forward	£450
Disposal	£150
	£300
Writing down allowance @ 25%	£ 75
Value carried forward	£225

The pool carried forward to 2001-2002 is £1,725.

COMMENCEMENTS AND CESSATIONS

If you started business between 6 April 1999 and 5 April 2001, your writing down allowance is calculated for the period of accounts which starts on the date that your business began.

Example 12
Bob starts business on 1 May 2000. He draws up his accounts to 31 December. On 1 May 2000 he buys a van for £12,000. He buys no other business assets. On 1 August 2001 he buys equipment costing £6,000. His capital allowance computation for his period of account ended 31 December 2000 is:

Cost of van	£12,000
Writing down allowance $^{8}/_{12}$ x 25%	£2,000
Value to carry forward	£10,000

His capital allowance computation for the period of account ended 31 December 2001 is:

Value brought forward	£10,000
Additions	£6,000
Writing down allowance 25% x £16,000	£4,000
Value to carry forward	£12,000

Bob has decided not to claim first year allowances

If your business ceases you should deduct from the value of the pool the sale prices for any items you sell, or their values if you keep them. If these are more than the value of the pool, the difference is a balancing charge. If there is any value remaining in the pool, do not work out a writing down allowance, but claim the value remaining as a balancing allowance, instead.

Example 13 shows how this is done. If you sell any items for more than you paid for them, or their value if you keep them is more than you paid for them, you should deduct the amount you paid for those items from the pool, and not the sale price or value. If you acquired the item from a connected person, you should deduct the greater of the cost to them and your cost if both are less than the sale proceeds.

Example 13
Jackson has been in business for many years. He draws up his accounts to 31 March. At 31 March 2000 the value in the pool is £10,000. He stops trading on 1 July 2000. He keeps a word processor with an open market value at 1 July 2000 of £2,000. He sells the other business assets for £7,000. His capital allowance computation for 2000-2001 is:

Writing down allowance brought forward	£10,000
Disposal proceeds (£7,000 + £2,000)	£9,000
Balancing allowance	£1,000

Special rules for particular items

The precise way the allowances for plant and machinery are worked out depends on the type of item and whether you use it privately as well as for business. The following rules will help you work out how much to claim under each of the headings in the Self-employment Pages.

— Expensive cars

For cars which cost more than £12,000, the 25% writing down allowance is restricted to £3,000 a year for each car. This amount is then restricted further if the car is used partly for private motoring. A separate calculation, as shown in Example 14, must be made for each car - they are not 'pooled'. If you sell the car, you do not get writing down allowances for the period of account in which the sale took place. Instead, you should calculate a balancing allowance or balancing charge. This is done in the same way as described in the sections on cessations above.

Example 14
Your accounts are drawn up for the year to 5 April 2001. You spend £15,000 in that year on a car which is driven 12,000 miles a year including 8,000 private miles. The calculation is:

Cost of car	£15,000
Writing down allowance @ 25% (restricted)	£3,000
Value to carry forward	£12,000
The writing down allowance you can claim is (£3,000 x 1/3 (one-third of mileage on business)).	£1,000

— Other cars

For cars which cost less than £12,000 and are used solely for business, separate calculations are not necessary. Instead, all expenditure and sales are dealt with in a single pool, separate from the pool of other capital expenditure. There is no restriction of the writing down allowance to £3,000.

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Any sales proceeds are deducted from the pool in the normal way. The pool continues until the last car in it is sold. When that happens no more writing down allowances are calculated but there is a balancing charge or balancing allowance.

— Plant and Machinery used only partly for business purposes

This category includes any cars costing less than £12,000 which are not used solely for business. These items should not be included in any pool. Instead the allowances on each item should be worked out separately (in the same way as Example 14) but there is no £3,000 restriction on the writing down allowance.

The writing down allowance, and any balancing allowance or charge when the item is sold, should be reduced so that only the business use proportion is taken into account.

Example 15

Your accounts are drawn up to 31 December each year. You buy a car for £8,000 in 1999 and sell it for £5,000 in 2000. You use it 50% for business. The calculation is:

1999-2000

Cost of car	£8,000
Writing down allowance @ 25%	£2,000
Value to carry forward	£6,000
The writing down allowance which can be claimed is (£2,000 x 50% business use).	£1,000

2000-2001

Value brought forward	£6,000
Price when sold	£5,000
Difference	£1,000
The balancing allowance which can be claimed is (£1,000 x 50% business use).	£500

— Short life assets

There are special rules if you intend to keep the item of equipment for only a short time or you think it will wear out quickly. If you acquire an item (other than a car) which you expect to dispose of within five years of the date you acquired it, you may elect to have the capital allowances calculated separately from your main pool.

You should make the election for this no later than the first anniversary of 31 January following the end of the tax year in which you acquired the item. You cannot withdraw an election. The separate calculation of capital allowances means that when the asset is sold the allowances given can be adjusted by way of a balancing allowance or charge to bring them in line with the actual depreciation.

If the item has not been sold or disposed of by the end of the five year period, the balance in the 'separate pool' for that item is added to the 'main pool', then dealt with in the normal way. Further information is available from your Inland Revenue office.

— Long life assets

A long life asset is an asset whose expected working life when new is more than 25 years.

The writing down allowance rate for long life assets is 6%. There is a separate pool of expenditure for long life assets and the 6% rate is applied to that pool. If you work full time in your business and the amount you spend on long life assets is less than £100,000, the reduced rate of writing down allowances does not apply.

— Assets leased out

You can claim capital allowances for assets you own and lease out to other users. Capital allowances on these assets should be claimed in the same way as for assets you use in your business. But first year allowance is not available on assets leased out. However, if the asset is used by a person who is not resident in the UK, you will need to discuss with your tax adviser what allowances are due.

Buildings

You can claim capital allowances for the cost of constructing agricultural or industrial buildings, industrial and commercial buildings in enterprise zones and certain types of hotel.

You can claim industrial buildings allowance if you buy or construct a building which is used for the purposes of a qualifying trade. Manufacturing is a qualifying trade, so are processing trades and there are certain others. You cannot claim industrial buildings allowance on buildings such as houses, showrooms, offices and shops even if they are used for the purposes of a qualifying trade, or for the land on which the building stands. You should consult your Inland Revenue office or tax adviser if you think you may be able to make a claim.

You can claim capital allowances at a special rate on industrial and commercial buildings in enterprise zones. You can also claim capital allowances for the cost of constructing a qualifying hotel or buying a qualifying hotel constructed on or after 12 April 1978. Ask your Inland Revenue office or tax adviser if you need help.

LOSSES

If your business ceased in 2000-2001 and you made a loss in your last year of trading, you can claim 'terminal loss relief' against any profits from the same business taxed in 1997-1998 or later. This is an alternative to the other ways in which losses can be relieved - for information on losses generally ask the Orderline for *Help Sheet IR227: Losses*. However, make sure that you do not claim the same loss twice.

TERMINAL LOSS RELIEF

If your business ceased in 2000-2001, you can set the loss of your final 12 months of trading against any profits from the same business which were taxed in 1997-1998, 1998-1999, 1999-2000 or 2000-2001.

The time limit for this claim is 31 January 2007.

First work out the amount of the loss from your final 12 months of trading (this is called the 'terminal loss'). If your 2000-2001 accounts cover a period of 12 months or more to the date your business ceased trading, the terminal loss is the allowable loss, or a 12 month proportion of the allowable loss.

Example 16
If your accounts covered 15 months to your cessation of trading on 31 October 2000, and the allowable loss is £5,000, your terminal loss is:

$£4{,}000 \left(£5{,}000 \times \frac{12}{15} \right)$

If your 2000-2001 accounts cover a period of less than 12 months, you need to add on part of the allowable loss from the 1999-2000 accounts to make the terminal loss up to 12 months.

Example 17
Your accounts covering six months to your cessation of trading on 30 September 2000, show a loss of £8,000. You had a loss of £7,500 in your accounts for the nine months to 31 March 2000. You need to add six months to bring your terminal loss to 12 months. You add onto your £8,000 loss £5,000 (£7,500 x $^{6}/_{9}$). So your terminal loss is £13,000.

The Working Sheet below will help you work out your terminal loss.

Allowable loss for 2000-2001

Either

a) if this account is more than 12 months, deduct a proportion of the loss to leave 12 months' worth of loss, **or** £

b) if this account is less than 12 months, add part of the allowable loss (if any) from earlier accounts to make up the 12 month period to the date your business ceased. £

Terminal loss £

If you have already claimed relief for the loss in (b) above then you must reduce the terminal loss by the amount of relief that you have already claimed. This is because you can only have relief once for each £1 of loss.

Your terminal loss must be set against any profits (after deducting losses brought forward) from the same business taxed in 2000-2001. If these are zero, it must be set against profits from the same business taxed in 1999-2000. Once these have been reduced to zero any balance of the terminal loss must be set against the profits taxed in 1998-1999. Finally, if there is still a balance, this must be set against the profits taxed in 1997-1998.

Enter the amount of terminal loss relief you are claiming against your 2000-2001 profits at box 3.85 or box 4.19 as a loss brought forward and used this year. This is in addition to any other losses you are bringing forward from earlier years, but make sure you do not count the same loss twice. Enter the total amount of terminal loss relief for 1999-2000, 1998-1999 or 1997-1998 in box 3.82 or box 4.16 and give details of the amount carried back to each year in the 'Additional information' box on Page SE4 of your Self-employment Pages.

If you have been sent your Tax Return for the year in which your business ceased then you must make your terminal loss relief claim in your Return. If you have not been sent your Tax Return yet then you can claim terminal loss relief as soon as you know how big the loss is, normally when the final accounts have been prepared for the business. If you wish to claim terminal loss relief before your Tax Return has been sent to you, write a letter.

Your letter should state:

- the name of your business
- that you wish to claim terminal loss relief
- the date your business ceased
- the profit or loss of the business from the end of the last basis period to the date the business ceased, calculated in accordance with the guidance in the Notes to the Self-employment Pages and elsewhere in this Help Sheet
- the terminal loss that you have calculated following the above guidance.

PARTNERS' TRADING OR PROFESSIONAL PROFITS

The basis period and overlap rules detailed above are applied to your share of the partnership's trading and professional profits (or losses) as if that income had arisen to you from **a business which you carried on alone**, as a sole trader.

That business will be deemed to have commenced on the date you became a partner (unless you previously carried on the business on your own account when it will be deemed to have commenced on the date you started the business) and deemed to have ceased on the date on which you ceased to be a partner (or if you carry on the business thereafter as a sole trader, on the date you cease to carry on that business).

continued over

Example 18: Basis period rules for partners

The partnership commenced business on 1 October 1998 and makes up its account each year to 30 September. You cease to be a partner on 31 December 2000. Your share of trading profits as shown in the Partnership Tax Return are as follows:

year ended 30 September 1999	£12,000	
year ended 30 September 2000	£18,000	(A)
year ended 30 September 2001	£7,000	(B)

Your basis periods for each fiscal year and the overlap relief to which you are entitled are as follows:

1998-1999	1.10.1998 to 5.4.1999	profits	£6,000	
1999-2000	1.10.1998 to 30.4.1999	profits	£12,000	
		(overlap profits	£6,000)	
2000-2001	1.10.1999 to 31.12.2000	profits	£25,000	(A) + (B)
	minus overlap relief		£6,000	(C)
	Taxable profit		£19,000	(D)

£18,000 should be entered in box 4.7 of the Partnership Pages, £7,000 in box 4.8, £6,000 in boxes 4.9 and 4.10 and £19,000 in boxes 4.13, 4.20 and 4.22.

If you are unsure how the basis rules apply to you, as a partner, ask your Inland Revenue office or tax adviser for help.

Other partnership income

The basis period rules to be applied to your share of the partnership's non trading or professional income are as follows:

If the partnership carried on a trade or profession in 2000-2001 then the basis period will depend on whether UK tax has been deducted from that income.

Your share of the partnership's non trading or professional income from which no UK tax has been deducted, 'untaxed income', is treated as having been derived from a second 'notional' business which you carried on alone. The same basis period and overlap rules which are applied to your share of the partnership's trading or professional profits are applied to the second 'notional' business which is treated as carrying on. But for this purpose the second 'notional' business is deemed always to have commenced on the date you became a partner and to have ceased on the date you ceased to be a partner.

Any overlap relief to which you may be entitled from your second 'notional' business is first to be relieved against any other untaxed income (regardless of the source from which it is derived) and the balance is to be given as a deduction against any other income of that year.

For your share of the partnership's non trading or professional income from which UK tax has been deducted 'taxed income' your basis period is the tax year. This is the period 6 April 2000 to 5 April 2001.

If the partnership did not carry on a trade or profession in 2000-2001 then your basis period for both 'untaxed' and 'taxed' income is the tax year. This is the period 6 April 2000 to 5 April 2001.

IR35 - THE PROVISION OF PERSONAL SERVICES THROUGH A PARTNERSHIP DEEMED SCHEDULE E PAYMENT

If the partnership provides a partner's services, or the services of others, to clients then new rules about tax and National Insurance contributions introduced from 6 April 2000 may apply. The rules will apply to the partner and the partnership if they can answer 'yes' to both the following questions:

- would the partner be an employee if they worked for the client directly and not through the partnership?
- does the partnership the partner works through, meet the conditions set out below?

The following conditions have to be met before the new rules can apply:

- the partner (or his/her family) is entitled to 60 per cent or more of the profits of the partnership, **or**
- all or most of the partnership's profits come from providing services to a single client, **or**
- the profit sharing arrangements in the partnership are designed to ensure that the partner receives an amount based upon the amounts received for their services to clients.

If the rules apply then the partner may have to pay an additional amount of tax and NICs, based on the payments received by the partnership for the partner's services, at the end of the tax year or earlier, if the partner ceases to be a partner during the year. This additional amount, which is known as a deemed payment, is treated as income from employment with the partnership. The partnership will need to apply PAYE and deduct NICs from this deemed payment. The partner will need to return this amount on a set of Employment pages in box 1.8, and record any tax deducted in box 1.11.

If the rules apply to the partnership then, in calculating its profits for tax purposes, a deduction is allowed for:

- the amount of the deemed payment, **and**
- the amount of any secondary Class 1 NICs paid on it.

The deduction is allowed once as a tax adjustment in calculating the taxable income of the partnership. Relief is given against the profits for the accounting period in which the deemed payment is treated as made (this will normally be 5 April) and is not to be apportioned between the partnership's accounting periods where the partnership makes up its accounts to a date other than 5 April.

The amount of the deduction allowed in calculating the Schedule D profits is limited to the amount that reduces those profits to nil. Therefore a deemed payment and the secondary NICs on that payment cannot create a Schedule D loss.

Where the partnership expenses incurred in respect of the relevant engagements exceed the sum of:

- the expenses allowable in calculating the deemed payment, **and**
- the 5% flat rate allowance allowable in calculating the deemed payment

then the excess amount is left out of account in calculating the Schedule D profits.

The adjustment for disallowable expenses should be made at box 3.66 of the Partnership Return. The amount of the deemed payment and any secondary Class 1 National Insurance contributions should be included at box 3.71 of the Partnership Return (if a deduction has already been made for any secondary Class I National Insurance contributions in the accounts, for example under employee costs, then that amount should be included in the figure at box 3.66). How you arrive at these figures should be entered in the 'Additional information' box, box 3.116 on page 3 of the Partnership Tax Return.

Further guidance on the new rules can be found in Inland Revenue leaflets *IR175: 'Supplying services through a limited company or partnership'*, and *IR2003: 'Supplying services: how to calculate the deemed payment'*.

Example 19: Deemed payment calculation

Mr and Mrs Jones carry on business in partnership and make up their accounts to 5 April 2001. All the partnership's income is derived from contracts covered by the new rules. Profits are split equally but Mrs Jones performs the services.

Partnership Accounts year ended 5 April 2001

Income	£20,000
Expenses (A)	£5,000
Profit	£15,000

Allocated Mrs Jones £7,500 and Mr Jones £7,500

Of the partnership's expenses, only £2,000 of the £5,000 would be allowable under Schedule E rules.

Calculation of deemed payment on 5 April 2001

Income from relevant engagements				£20,000
Minus	5% flat rate allowance (£20,000 x 5%) (B)		£1,000	
	Schedule E expenses (C)		£2,000	
	Secondary Class 1 NICs on deemed payment		£1,372	£4,372
	Deemed payment			£15,628

Recalculation of partnership's taxable profit

	Partnership profit	(enter at box 3.65)		£15,000	
Plus	Disallowed expenses				
	A *minus* (B + C) £5,000 *minus* (£2,000 + £1,000)	(enter at box 3.66)		+ £2,000	**Note**: The disallowed expenses are the excess of the partnership expenses in the accounts (A) over the sum of the Schedule E expenses (B) and 5% flat rate allowance (C).
Minus	Secondary Class 1 NICs on deemed payment			- £1,372	
	Deemed payment	(enter at box 3.71)		£15,628	**Note:** The deemed payment amount is restricted to an amount that reduces the Schedule D profit to zero '0'.
	Taxable Schedule D profit	(enter at box 3.73)		0	

These notes are for guidance only, and reflect the position at the time of writing. They do not affect any rights of appeal.